CBA | CONSUMER BANKERS ASSOCIATION

December 15, 2005

Jennifer J. Johnson, Secretary
Board of Governors of the Federal Reserve System
20th Street & Constitution Avenue, N.W.
Washington, D.C. 20551

Re: Docket No. R-1217: Second Advance Notice of Proposed Rulemaking - Regulation Z Open-End Credit Disclosures

Dear Ms. Johnson:

The Consumer Bankers Association (CBA)[1] is pleased to submit these comments on the supplementary ANPR concerning open-end credit disclosures under Regulation Z.

Overall:

Congress has acted, in the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (Bankruptcy Act), to require a number of new disclosures in connection with consumer credit transactions, mostly with respect to open-end credit. CBA concurs with the Board's plan to combine the rulemaking called for under the Bankruptcy Act with the ANPR already underway for review of the open-end credit rules in Regulation Z. Separate regulatory treatment of the new Bankruptcy Act requirements, either ahead of or behind the overall open-end review would be inefficient and probably slower than an integrated process. We also concur that it would be unwise to proceed with revision or adjustments to the "clear and conspicuous" standard in a vacuum, before the substantive disclosure rules are settled.

The major component of the new Bankruptcy Act requirements relates to disclosures concerning the length of time needed to pay off an open-end balance if the consumer makes only minimum payments. Available data suggests that the number of consumers who regularly make minimum, or close to minimum, payments is small. And whether a new disclosure will affect consumer behavior in this regard is untested. Thus one obvious concern for CBA members is that the new

[1] The Consumer Bankers Association is the recognized voice on retail banking issues in the nation's capital. Member institutions are the leaders in consumer finance (auto, credit cards, home equity and education), electronic retail delivery systems, bank sales of investment products, small business services, and community development. CBA was founded in 1919 and provides leadership and representation on retail banking issues such as privacy, fair lending, and consumer protection legislation/regulation. CBA members include 85% of the nation's 50 largest bank holding companies and hold two-thirds of the industry's total assets.

disclosure requirement not become an unwarranted burden of expense and compliance complexity. Keep it simple, and to the point.

The point, we believe, is to provide consumers with a piece of information – a hypothetical payoff term - that would result from a completely unlikely pattern of consumer conduct - minimum payments with no other account activity - to allow consumers to make choices about periodic repayment amounts. It cannot have been Congress' intent to *prohibit* small minimum payments or long amortizations; Congress could easily have regulated those matters directly. For some consumers, a pattern of minimum payments could be a very prudent allocation of resources, as during an introductory rate period, or when they have more urgent demands on their cash flow. Thus the regulatory objective should be to produce a disclosure that helps consumers make choices, and not a disclosure that purports to predict an actual or realistic pattern of conduct. It is the nature of open-end credit that it does not have a fixed amortization schedule, and the new disclosures should not suggest or assume otherwise.

The Bankruptcy Act focuses on two levels of disclosure accuracy. One is an estimated payoff period, derived from tables prepared by the Board.[2] The other is a *supposedly* actual projection of the payoff period, based on the actual terms and features of the account. Some issuers may be content to rely on the estimated disclosures based on Board tables because they would provide a built-in compliance safe harbor. But we are hearing considerable interest on the part of CBA members to adopt the "actual" approach, giving consumers a more precise payoff projection, avoiding reliance on consumer inputting of critical data, and relaxing the front page format requirements that apply to certain of the disclosures concerning estimates. However, this approach would find no favor without a safe harbor for the issuer who relies on certain basic assumptions in its calculation and disclosure.

Possible Exemptions: Q59-Q61

As to Q59, we understand that the legislative history of the Bankruptcy Act centers on concerns about credit card repayment, virtually to the exclusion of other forms of consumer credit. We believe there are appropriate grounds to exclude several types of open-end credit:

Home equity lines of credit (HELOCs) almost always have a contractual limit on the "draw period" under the plan, with the outstanding balance payable at the end of that time or according to a fixed schedule of repayment thereafter. Since these arrangements dictate that all outstanding balances are due on a certain date or dates, it is not useful, or mathematically proper, to project a repayment schedule based solely on minimum payments. Moreover, Regulation Z already calls for extensive disclosures about payment obligations on a HELOC, including a $10,000 example

---

[2] We assume that a creditor could program into its data systems the payoff period formula that is implicit in the Board "tables," and respond to customer inquiries by applying that formula to the information furnished by the consumer from his/her periodic statement.

that factors in both minimum payments and any resulting balloon payment obligation. Regulation Z § 226.5b(d)(5)(iii).

Overdraft checking plans do not involve credit cards, and repayment obligations are typically based on subsequent deposits to the account rather than customer-selected payment amounts. A long-term pattern of "minimum payments" is unlikely in these plans.

There may be other patterns of open-end credit that do not involve a credit card as such, where the repayment obligation is not stated in terms of minimum periodic payments.

We believe it would be consistent with the congressional purpose to limit the new disclosures to those plans presently covered by Regulation Z 226.5a (with the exception of charge cards that do not permit revolving balances or deferred repayment[3]).

With respect to Q60, we suggest that creditors have the option not to make payoff period disclosures to certain categories of consumers, presumably those who are not likely to make minimum payments for any extended periods of time. The question is how to identify those persons. Since past performance is the best predictor of future conduct, a plausible basis for exclusion would be to exclude consumers who have made more than minimum payments on balances outstanding in a specified number of months, perhaps three.

Hypothetical Examples on Periodic Statements: Q62–Q64

Although the 17% APR used in the statutory examples is at the high end of prevailing rates, we do not encourage the Board to change it at this time [Q62]. An immediate change from the statutory example suggests that the rate used in the disclosed example should be changed frequently to reflect the current market. This requires constant - and expensive - revision and re-printing of forms, and the regulation would probably need to provide detailed rules on transitioning disclosures from one rate example to another. If the value of this disclosure item lies partly in its shock value, then an assumed high rate reinforces that shock.

We have urged above that these new disclosures be limited to credit card plans. If, however, HELOCs or other non-card open-end plans are included, examples that accord to the scale of those plans would be appropriate. [Q63].

As to Q64, we strongly urge the Board not to feel constrained to require the use of statutory language in the actual language of the disclosure. Congress writes to set the policy, while the consumer disclosures are to transmit understandable information to people. Any language that fairly indicates that the example is built on a hypothetical should suffice: "typical" may do that,

[3] Remarks of Senator Grassley (2005), *Congressional Record* (daily edition), vol. 151, March 1, p. S 1856

but so might "for example . . ." or "assuming . . ." or other formulations. It is hardly in the creditor's interest to mislead or create confusion for its customer in this shock-value example.

<u>Assumptions to be Used in Calculating Repayment Period</u>: Q65

In sum, we agree that the relevant assumptions built into the statutory examples should be carried forward into the formulas used for estimated payoff periods. These include [Q65]:

A previous balance calculation method;
No grace period;
No residual interest.

The Board's senior economist has circulated a paper analyzing the assumption options. We support his conclusions. Anything more complex than these assumptions risks making the Board "tables" almost unmanageable.

If the "estimated" payoff period disclosure in response to customer inquiry is to have any utility, or any integrity, the consumer must be able to input the critical variables such as account balances and rates without undue difficulty and based presumably on the customer's most recent periodic statement. We are not entirely optimistic that consumers will be able, easily, to identify and enter correctly the several different combinations of balances, rates, and minimum payments necessary to prompt a reliable estimate. Even if the consumer dutifully entered the correct amount for this months minimum payment, that does not shed light on the formula used to calculate that payment, nor on what the minimum payment will be the next month, or the month after that. Our view is that some set of assumptions, especially about minimum payment calculations, must be built into the Board tables and the formulas underlying them. A banking industry approach may be centering on formulas encouraged by bank regulators, such as 1% of the principal balance plus accrued finance charges. [Q66, Q67]. A different assumption may be justifiable for retailer cards, but we take no position on what it should be. Any such assumed formula should not be one that allows negative amortization. [Q69].

What emerges from the Board's ANPR is an appreciation for a gradation of estimates about payoff periods. The first rough approximation is in the statutory example to be disclosed on the front of the periodic statement. The second approximation is the response to the customer's phone inquiry, which uses some assumptions and some account-specific information. The third level is what the statute and the Board characterize as an "actual" projection, discussed below in connection with Q77–Q79. This latter projection is no more "actual" than any other speculation about an unlikely payment pattern. But it is the most refined, and therefore the most accurate, estimate of what a minimum payment pattern would look like. We hope the Board will provide incentives and authorizations "safe harbor" that encourage widespread use of an "actual," or "best estimate" approach.

<u>APR Information</u>: Q70–Q75

Almost all bank cards have at least two APRs running, one for cash advances, another for purchases. With introductory rates, and promotions for balance transfers, and the like, there are often three or more APRs applicable to account balances [Q70]. Our concerns, above, about the ability of consumers accurately to discern and enter multiple rates, and to identify the subtotals of account balances to which each rate applies, are heightened if the "estimate" disclosure must take account of multiple rates and balances. It would seem almost impossible to prepare tables to estimate a single composite payoff period with all these variables. Our somewhat grudging conclusion is that the estimate exercise should use a single APR, which might be the highest used in the plan (which would produce the longest payoff period) [Q71].

The Board's questions Q72 through Q76 suggest the possibility of extensive *additional* disclosures, not required by the statute, including multiple payoff projections (to account for multiple rates), subtotals of the account balance, and disclosures of the assumptions built into the estimates. This, we believe, is exactly the *wrong* way to go to implement the Bankruptcy Act requirements. It tends to elevate these current additions to the long-standing TILA disclosure structure to a position of predominance, as if this payoff projection is somehow the most important disclosure, deserving of center stage. We respectfully and strongly disagree that the time-tested disclosures of credit costs should be subordinated, or overwhelmed, by a single informational item of doubtful relevance to most open-end credit customers.

<u>Option to Provide "Actual" Months to Repay</u>: Q77–Q82

As we have suggested at several points, we believe the Board would be wise to develop proposals that would encourage and facilitate the disclosure of an "actual" repayment projection. "Actual" in this sense cannot be taken literally; rather it would be a "best estimate" because it would be based on the actual features and terms of the plan. The benefit of such an approach - if it can be done in an effective way - is that it would reduce the number of arbitrary assumptions to a minimum, and ease the burden on the consumer to enter accurately a number of pieces of data from a periodic statement. All the consumer would need to provide is an account number.

We believe that the Board should provide appropriate assumptions and/or safe harbors in providing the "actual" option. [Q77], because without them, the degree of inaccuracy inherent in attempting to provide this disclosure will render this alternative too risky to use. It appears to us that there at least four items of information that are most important with respect to determining the "actual" number of months to repay the balance making only the minimum payments, namely (i) the account balance, (ii) the applicable interest rate or rates and the portions of the balance to which such rates apply, (iii) the minimum payment computation, and (iv) any flat alternate minimum payment. Additionally, certain basic assumptions work together with these basic items of information, namely (i) assuming the account has no new transaction or charges, (ii) assuming that the rate does not change, (iii) ignoring late charges, overlimit fees, and other charges on the account, and (iv) assuming the disclosure is given as of the most recently passed statement closing date for which information is readily available from the financial institution's system (rather than requiring disclosures utilizing information derived mid-billing cycle). Whether these alone, or certain other items of information and/or assumptions are the most important in determining the number of months, we believe that the Board should create a safe harbor that stipulates that any number of months correctly calculated (i.e., *"correctly"* in the sense of avoiding mathematical errors) using these limited number of important items and assumptions will be deemed to be accurate, nothwithstanding differences that may occur from one computation to another because of other less important factors or assumptions, such as the balance computation method, the payment due date, the method of allocating payments, when payments are actually received, the number of days in a month, and so on.

In addition, we urge the Board to develop a proposal such as is suggested in Q82. If creditor systems can generate "actual" payoff projections, creditors may prefer to disclose that information routinely, on the periodic statement, rather than maintain the infrastructure necessary to respond to telephone inquiries. Creditors that choose this option should be exempted from not only the toll-free number requirement, but also from the front-page hypothetical example.

<u>Introductory Rates: Q85-Q92</u>

The Board asks a series of questions about appropriate applications of the "clear and conspicuous" standard to the newly required disclosures about introductory or "teaser" rates. We acknowledge the need to follow the statutory directions on these matters, and it is true that creditors often seek bright-line, safe harbor guidance on disclosure format. Nonetheless, we question the need for endlessly hair-splitting verbal distinctions to try to set precise boundaries among terms such as "reasonably understandable," "immediate proximity," "prominent location," "closely proximate," "prominent manner," "general description," and "first mention." At some point the quest for precision becomes almost picayune, or stultifying with respect to efficient forms design. We concur with the Board's suggestion that further refinement of "clear and conspicuous" standards should be deferred pending notice and comment on the pending Regulation Z review.

<u>Internet Based Card Solicitations</u>: Q93-Q96

Since card solicitations and applications must be treated alike when marketed in paper form, there seems no reason not to treat them alike in the Internet environment [Q93]. The issues of conspicuousness and "accessibility" [Q94, Q95] should be part of the larger effort to harmonize a general principle of transparency in all the open-end disclosures. In general, we believe the 2001 interim rules on electronic disclosure are working well; at very least they provide a platform for responding to the new Bankruptcy Act requirements.

Payment Deadlines & Late Payment Penalties: Q97-Q101

For the most part, we believe the Bankruptcy Act requirement for late fee disclosure codifies prevailing practices in the marketplace [Q97]. Virtually all open-end plans, and the periodic statements under them, tell customers the payment due date, say April 30, and then provide a grace period before a late payment fee will be charged, say on May 10. The issue of the form and location of these disclosures should be treated as part of the larger conspicuousness policy.

As to Q99, concerning cut-off hours for crediting payments, banks may have different cut-off hours depending how and where payments are made, e.g., there may be one cut-off hour for payments by traditional mail, another for Internet payments, and yet a third for ACH transfers. It would be very difficult to disclose a single cut-off hour for the bank, and unduly cumbersome to try to disclose a series of cut-off hour variations. The existing requirement that cut-off hours be "reasonable" should be a sufficient restraint on any potential abuse.

Home Secured Loans That Exceed Dwelling's FMV: Q102-Q105

We believe that the new disclosure concerning the deductibility of mortgage interest only makes sense when the creditor has reason to know that the current extension of credit, in and of itself, will exceed a recently appraised value of the dwelling. If the creditor must give these disclosures whenever the debtor's *aggregate* mortgage debt may exceed the home value, creditors have no easy way to verify these numbers without confirming the outstanding balances on all other mortgage loans, and getting a new appraisal. This information *may* be generated as part of the creditor's underwriting, but not necessarily so, as for example in low- or no-doc loans. To cope with this, creditors would need to give the disclosures in every single mortgage transaction, even where it has no relevance, and it will become a meaningless piece of boilerplate. Moreover, the notice is literally accurate only when the current loan, by itself, exceeds the home value; otherwise, only some portion of the aggregate loan interest may not be deductible, not necessarily all attributed to the new loan.

Terminating Accounts for Failure to Incur Finance Charges: Q106-Q108

We believe the expiration date stated on the card could be considered the default "expiration date," even though it may serve primarily a security function [Q106]. That is, it would control, for purposes of the new Bankruptcy Act prohibition on account cancellation, unless there was a separate expiration date stated in the parties' contract.

The exception for "inactivity" should apply whenever the account has been essentially dormant for three or more months, i.e., no payments and no new charges. It is the absence of customer activity that should control.

* * *

Thank you for considering these comments. CBA will be pleased to provide any additional information, and to work with Board staff on formulating concrete regulatory proposals as a result of this ANPR.

If you need further information, please contact me at (703)276-3871, Joe Crouse at (703)276-3869, or Ralph Rohner at (202)319-6753.

Sincerely,

Steve Zeisel
Vice President & Senior Counsel